Supreme Court of the United States.

No. 91.—October Term, 1905.

Fred H. Kolze, Administrator, etc., et al., Appellants, *vs.* Charlotte E. Hoadley.	Appeal from the Circuit Court of the United States for the Northern District of Illinois.

[January 2, 1906.]

This was an appeal from a decree of the Circuit Court in favor of the plaintiff, Charlotte E. Hoadley, a citizen of Massachusetts, against Abraham L. Day and other defendants, among whom were Fred H. Kolze, administrator of the estate of Frederich Kolze, deceased; Lina Kolze, his widow; Louisa Kolze, his daughter, and Charles E. Stade, trustee, all citizens of Illinois, foreclosing three trust deeds given by Day to secure promissory notes in the aggregate amount of $5,400. The appeal was granted solely upon the question of jurisdiction.

The point involved requires a statement of facts at some length. They are substantially as follows:

Frederich Kolze sold and conveyed certain real estate to Day by warranty deed dated and acknowledged November 15, 1897, for a stated consideration of $45,000, namely, $1,000 in cash and the remainder in notes secured by trust deeds. To secure such notes Day executed three trust deeds to one Stade as trustee, conveying the real estate in question, which were dated November 17 and acknowledged and recorded November 24, 1897. Kolze thereupon intrusted the notes and trust deeds to Stade, a nephew, in whom he seemed to have great confidence, the notes being executed by Day to his own order and by him indorsed in blank.

On February 17, 1898, Stade took the notes and trust deeds securing the same and pledged them to Charlotte E. Hoadley as collateral security to his own notes, upon which Hoadley then advanced, or secured to be advanced, a large sum of money.

By deed dated and acknowledged November 23, 1897, but not delivered or recorded until June 30, 1898, Day reconveyed the premises to Kolze, and by deed of release, dated and acknowledged October 27, 1898, and recorded October 29, 1898, Stade as trustee fraudulently released said three trust deeds to Kolze, reciting a consideration of one dollar and other valuable considerations, and further reciting that the notes secured thereby had been cancelled.

By deed dated October 29, 1898, Kolze, now deceased, and the appellant, Lina Kolze, his wife, conveyed said premises to Louisa Kolze, their daughter,

upon an expressed consideration of $12,000, although the grantee was not a *bona fide* purchaser, and said conveyance was made to her to hold for the benefit of the family.

For the ostensible purpose of securing the payment of the purchase money, said Louisa Kolze executed a trust deed to secure her promissory note of $10,000, to Percy V. Castle, as trustee. This deed was dated October 27, 1898, acknowledged October 28, 1898, and recorded October 29, 1898, the appellant Fred H. Kolze, as administrator of the estate of his father, being the owner of said notes and trust deeds, subject, as was alleged, to the rights of the plaintiff Hoadley.

Subsequently, on or about April 21, 1899, the notes and trust deeds of Day, upon default by Stade in the payment of his note, were sold in accordance with the terms of the collateral note, and were bought in by and became the property of the appellee Hoadley.

The bill prayed that the release deed executed by Stade to Fredrich Kolze be declared fraudulent and void as against the notes and trust deeds executed by Day and now owned by the plaintiff; that the rights of all the defendants be declared subject to those of the plaintiff under the notes and deeds held by her; that a receiver be appointed and an account had, and the defendants be decreed to pay whatever was due under the notes and trust deeds, and in default thereof that the premises be sold and the defendants be held liable for any deficiency upon such sale, and that they all be foreclosed of their right of redemption.

The defendants moved to dismiss the amended bill for want of a proper allegation of diversity of citizenship, which was overruled; and thereupon defendants interposed a plea to the jurisdiction upon the ground that the defendants were all citizens of the State of Illinois; that the suit was brought by plaintiff as the assignee of one William P. Smith, to whom the notes had been hypothecated by Stade to secure his, (Stade's) note, and also to secure Smith for the faithful performance by Stade of a certain contract of employment; that upon the failure of Stade to pay his note and carry out his contract said mortgage notes and trust deeds signed by Day were sold on or about April 21, 1899, and were bought in by and became the property of the plaintiff; that Stade and Smith, "the successive assignors" of the appellee, were citizens of the State of Illinois, the same State of which Day, the maker of the notes was also a resident, and that by reason of the fact that said suit could not have been prosecuted in a Federal Court, if no transfer or assignment had been made, the Circuit Court had no jurisdiction of the case.

This plea was held to be insufficient, and the defendants failing to answer, were defaulted, and a decree thereafter entered to the effect that Stade as trustee had frandulently released the trust deeds; that the trust deeds

were valid as liens upon the premises; that the rights of Louisa Kolze, subsequent grantee under the warranty deed, as well as the deed of Kolze, were subject and subsequent to the rights of the plaintiff as the owner of the notes and deeds signed by Day; that the property be sold and the defendants foreclosed of their equity of redemption.

Thereupon defendants appealed to this Court solely upon the question of jurisdiction.

Mr. Justice BROWN delivered the opinion of the Court.

The sole question presented by the record in this case is whether this is a suit to recover the contents of a chose in action, in favor of an assignee, which could not have been prosecuted if no assignment or transfer had been made.

By section 1 of the Act of August 13, 1888, it is provided that no Circuit nor District Court "shall have cognizance of any suit . . . to recover the contents of any promissory note or chose in action in favor of any assignee, or of any subsequent holder, . . . unless such suit might have been prosecuted in such court to recover the said contents, if no assignment or transfer had been made." This language is taken from the original Judiciary Act of 1789, and has been in force, except for a few years, since the foundation of the Government.

In construing this clause the decisions of this Court have settled the following propositions:

1. That a suit to recover the *contents* of a promissory note or other chose in action is a suit to recover the amount due upon such note, or the amount claimed to be due upon an account, personal contract, or other chose in action. (*Serè* v. *Pitot*, 6 Cranch, 332; *Deshler* v. *Dodge*, 16 How. 622, 631; *Bushnell* v. *Kennedy*, 9 Wall. 387; *Shoecraft* v. *Bloxham*, 124 U. S. 730.)

In *Corbin* v. *County of Blackhawk*, (105 U. S. 659,) a suit to compel the specific performance of a contract was held to be within the statute, Mr. Justice Blatchford observing (page 665): "The contents of a contract, as a chose in action, in the sense of section 629, are the rights created by it in favor of a party in whose behalf stipulations are made in it which he has a right to enforce in a suit founded on the contract; and a suit to enforce such stipulations is a suit to recover such contents."

2. That a suit to foreclose a mortgage is within the inhibition of the act, and can only be maintained where the assignor was competent to file the bill. (*Sheldon* v. *Sill*, 8 How. 441; *Blacklock* v. *Small*, 127 U. S. 96.)

3. That the bill or other pleading must contain an averment showing that the suit could have been maintained by the assignor if no assignment had been made. (*Turner* v. *Bank of North America*, 4 Dall. 8; *Mullan* v. *Torrance*, 9 Wheat. 537; *Bradley* v. *Ryan, Administrator*, 8 Wall. 398;

Anderson v. *Watt*, 138 U. S. 694, 702; *Robertson* v. *Cease*, 97 U. S. 649; *Brock* v. *Northwestern Fuel Co.*, 130 U. S. 341.)

4. That a suit may be maintained between the immediate parties to a promissory note as indorser and indorsee, provided the requisite diversity of citizenship appears as between them, or upon a new contract arising subsequently to the execution of the original, notwithstanding a suit could not have been maintained upon the original contract. In such case the original contract may be considered to ascertain the amount of the damages. (*Young* v. *Bryan*, 6 Wheat. 146; *Bank of United States* v. *Moss*, 6 How. 31; *City of Superior* v. *Ripley*, 130 U. S. 93; *Mullan* v. *Torrance*, 9 Wheat. 537; *Manufacturing Company* v. *Bradley*, 105 U. S. 175.)

This is primarily a suit to foreclose certain mortgages. Instead of setting up the mortgages, their maturity and non-payment, and their assignment to plaintiff, leaving to the defendants to plead the release by Stade of October, 1898, as an extinguishment of the mortgages, she has chosen to set forth the entire facts, to attack the release as fraudulent as against her, and to insist that the original notes and trust deeds are valid in her hands, and to pray for a foreclosure of the same.

The gravamen of the suit and the object to be attained are unaffected by the form of her bill. The suit is still in substance a suit to foreclose the trust deeds, and to remove the release as a cloud upon her title to them.

It may be that an action for fraud might have lain against the parties implicated, regardless of the citizenship of the parties from whom the plaintiff traced her title, or possibly a bill in equity to cancel the release deed of Stade and remove a cloud from the title. But where a bill is filed to foreclose a mortgage, and it appears by the bill itself that the mortgage has been fraudulently released to the mortgagor by a deed of which plaintiff had no notice, and the fraud is a mere incident, the bill is still one to recover the contents of a mortgage within the meaning of the act, and will not lie in a Federal Court unless the plaintiff's assignor might have maintained the bill, if no assignment or transfer had been made. It would advantage the plaintiff nothing to obtain a cancellation of the release without also foreclosing the mortgage in the same or a subsequent suit, while a right to foreclose the mortgage could not be established without incidentally avoiding the release.

In this aspect of the case it would seem to be immaterial whether the plaintiff derived her title directly from Stade, to whom she had advanced money and afterwards purchased the notes and trust deeds, as alleged in the bill, or through William P. Smith, who had obtained the notes and trust deeds from Stade, his debtor, since both Stade and Smith were citizens of the State of Illinois, and the inhibition of the statute would apply in either case.

The case of *Blacklock* v. *Small*, 127 U. S. 97, is similar, and we think practically decisive of the one under consideration. A suit was brought in the Circuit Court for South Carolina by two daughters of John F. Blacklock, who were citizens of Georgia, against certain defendants, who were citizens of South Carolina. It seems that Blacklock had sold a house and lot in Charleston to the defendant Small, who had given back a bond and mortgage to secure a portion of the purchase money; that Blacklock subsequently assigned the bond to Alexander Robinson in trust, for his (Blacklock's) children; that Small pretended to pay the bond by making payment to Robinson in Confederate treasury notes; that upon receipt thereof, Robinson satisfied the mortgage and delivered up the bond to Small; that Robinson, in receiving such payment, violated his duty, and was guilty of a breach of trust; that Small, in attempting to pay the debt in illegal currency, with full notice of the trust, had not paid the debt; that the satisfaction of the mortgage was void; that its lien was still subsisting, and that Small was still liable for the amount due upon the bond. It was held that, as the suit was one against Small, founded upon contract, namely, his bond and mortgage in favor of plaintiffs, who claimed only under the assignment made by their father, John F. Blacklock, to the defendant Robinson, such suit would not lie, inasmuch as plaintiff's assignor, John F. Blacklock, was a citizen of South Carolina and of the same State as Small. In answer to this it was insisted that the suit should not be considered as one founded upon the contract of Small, but as one for the delivery of the bond and mortgage by Small to the plaintiffs, founded on their wrongful detention, and that the foreclosure and sale of the premises prayed for was merely ancillary and incidental. The contention was held to be unsound, Mr. Justice Blatchford saying that the bill was clearly one for a decree for the amount of the bond and a sale of the mortgaged premises. In other words, the foreclosure and sale were treated as the main objects of the bill, and the breach of trust of Small as a mere incident. The cases of *Deshler* v. *Dodge*, (16 How. 622,) and *Bushnell* v. *Kennedy*, (9 Wall. 387,) were cited and distinguished.

By analogy to *Blacklock* v. *Small*, we think the gravamen of this case must be treated as the foreclosure of the trust deeds in question, and the prayer for a cancellation of the release given by Stade to Frederich Kolze as a mere clearing of the way to a decree establishing the title of the plaintiff to the notes and trust deeds. As the plaintiff is thus compelled to trace her title through Stade or Smith, who are both citizens of Illinois, and neither of whom could have prosecuted this suit, she is affected by the same incompetency.

The case of *Holmes* v. *Goldsmith*, (147 U. S. 150,) on which the plaintiff relies, is not in point. That was an action by a non-resident against the maker of a note, who had signed it entirely for the benefit of the payee,

with by an order. This therefore is not one of those irregularities that can be waived by taking a step in the cause, but an erroneous proceeding, contrary to the established course of the court, making the record imperfect, as in the instance of a bill or answer without the signature of counsel."

As a plea, under the rulings of this court, the plea filed by appellants could properly have been disregarded.

In *National Bank* v. *Insurance Co.*, 104 U. S., 54, this court say:

"It is also assigned for error that the appellee failed to set down for argument or traverse the pleas of the defendant, as required by the thirty-eighth equity rule; but the pleas in this case were irregularly filed and defective, under the thirty-first rule, for lack of the affidavit of the defendant that they were not interposed for delay, and of the certificate of counsel that they were, in his opinion, well founded in point of law, and may well have been disregarded on that account."

While the plea in this case might thus have been disregarded, such a practice under the rules seems a dangerous one.

Rule 33 provides that "the plaintiff may set down the demurrer or plea to be argued, or he may take issue on the plea," thus giving him but two alternatives; and Rule 38 provides: "If the plaintiff shall not reply to any plea, or set down any plea or demurrer for argument, on the rule day when the same is filed, or on the next succeeding rule day, he shall be deemed to admit the truth and sufficiency thereof, and his bill shall be dismissed as of course, unless a judge of the court shall allow him further time for the purpose."

So that the only course apparently provided by the

rules for a plaintiff is to call up the plea and obtain a ruling thereon.

Smith is not mentioned in the bill of complaint or in the decree.

The allegations of the bill are that Kolze entrusted the notes "endorsed in blank, and being therefore negotiable by delivery, together with said trust deeds, now owned by your oratrix, to the said Charles E. Stade, *his trusted agent* in the premises, for safe keeping; and your oratrix shows that while the same were in the custody and keeping of the said Charles E. Stade, *as the agent* of the said Friedrich Kolze, but with all the indicia of ownership of the said securities, your oratrix, on or about the 17th day of February, A. D. 1898, advanced or secured to be advanced a large sum of money upon the note of said Charles E. Stade, secured to be paid by the pledge of the said nine principal notes and three trust deeds as collateral security therefor, and the said nine promissory notes and three trust deeds were then and there deposited by the said Charles E. Stade as such collateral security, and were relied upon by your oratrix as security for the sum of money advanced or secured to be advanced by your oratrix, as aforesaid; and your oratrix shows that the note of the said Charles E. Stade, to secure which the said nine promissory notes and three trust deeds were deposited, as aforesaid, was not paid in whole or in part, and said nine promissory notes and three trust deeds were thereafter sold, in accordance with the terms of the said collateral note, and were bid in and became and now are the property of your oratrix, and your oratrix is now the legal owner and holder thereof." (Rec., 11.)

The decree recites (Rec., 38) that the cause came on to be heard upon the report of William M. Booth, master in chancery, and the exceptions thereto, and that the court had heard arguments of counsel for the respective parties herein, and had fully considered the said master's report, and the exceptions thereto, and that the exceptions were overruled and the report approved; it then contains a finding that the material allegations in the amended bill of complaint contained, are true as therein stated.

Thus the bill traces the notes directly from Kolze, through Stade, his agent, to the appellee. The evidence proved this material allegation, as was evidently reported by the master and considered by the court, with all the facts before it, and as is found by the decree.

Appellants recognized that Smith did not figure in the question of want of diversity of citizenship presented by the record, as is shown by the language of their motion filed on January 14, 1904, in which Smith is not mentioned, and the claim is made that "it does not appear either from the original bills of complaint or from said amended bill of complaint, that the proper diversity of citizenship existed at the time of the commencement of the said suits, thereafter consolidated, between Friedrich Kolze, alleged in said amended bill of complaint to have been the original owner of the nine promissory notes and the three trust deeds securing the same, in said amended bill of complaint described, or said Charles E. Stade therein alleged to be his trusted agent in the premises, the assignors of said Charlotte E. Hoadley, complainant, and the defendants,

or any of them, so as to confer jurisdiction," etc. (Rec., 629.)

So, also, in their assignment of errors, appellants disregarded the allegations relating to Smith, in their plea, assigning as error denial of the motion to dismiss the amended bill "for want of jurisdiction because it did not appear that the proper diversity of citizenship existed at the time of the commencement of the said suits thereafter consolidated, between Friedrich Kolze or Charles E. Stade, alleged to be his agent, the assignors of said Charlotte E. Hoadley, complainant, and the defendants, or any of them, so as to confer jurisdiction," etc., and also in overruling the plea, "said plea being to the jurisdiction of said court *for the reason above stated.*"

But even if Stade had pledged the notes and trust deeds to Smith (which was not the fact and is not shown by the record), the title to the papers would not have passed to Smith, and would not have passed out of Kolze, the owner, until a valid sale under the collateral note.

The character and effect of a pledge is thus stated in Jones on Pledges and Collateral Security, 2d Ed., Sec. 7:

"A pledge differs from a mortgage of personal property in being a lien upon property and not a legal title to it; and the pledgee's especial property in the pledge is not enlarged by the pledgor's default in paying the debt, secured at its maturity. *The legal title to property pledged remains in the pledgor,* while a mortgage passes the legal title of the property itself to the mortgagee, subject to be revested in the mortgagor, upon the performance of an express condition subsequent."

who was really the party for whose use it was made. The maker and payee were citizens of the same State. The plaintiff, a *bona fide* holder, had paid full value for it to the payee, who had indorsed it to him. It was held the Court had jurisdiction; that evidence showing the real relation of the parties was admissible, and that the jurisdiction of the Circuit Court "was properly put by the Court below upon the proposition that the true meaning of the restriction in question was not disturbed by permitting the plaintiffs to show that, notwithstanding the terms of the note, the payee was really a maker or original promissor, and did not, by his indorsement, assign or transfer any right of action held by him against the accommodation makers."

The decree of the Circuit Court is therefore reversed, and the case remanded to that Court with instructions to dismiss the bill.

True copy.

Test:

Clerk Supreme Court, U. S.